Nos. 95-596, 95-606

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

LEP GROUP PLC, WILLIAM R. BERKLEY, and PETER J. GRANT,

Petitioners,

—v.—

ITOBA LIMITED,

Respondent.

ON PETITIONS FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

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STATEMENT PURSUANT TO RULE 29.6 OF THE RULES OF THE SUPREME COURT OF THE UNITED STATES

Respondent Itoba Limited ("Itoba") is the wholly-owned subsidiary of A.D.T. Limited, a Bermudan corporation the shares of which are listed on the New York Stock Exchange. Itoba has no nonwholly owned subsidiaries.

JURISDICTION

Pursuant to Rule 24.2 of the Rules of this Court, respondent states that it is dissatisfied with the statement in the Petition filed by William A. Berkley and Peter J. Grant that "[t]he jurisdiction of the district court was invoked under 15 U.S.C. § 78c(17)." The Complaint alleges jurisdiction of the District Court under Section 27 of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa.

COUNTER-STATEMENT OF QUESTIONS PRESENTED

1. Should the Court grant *certiorari* to review an interlocutory decision remanding the case to the District Court for further factual development of jurisdictional issues?

2. Should the Court grant *certiorari* when there is no conflict among the Circuits, which all apply a substantially similar Conduct Test/Effects Test analysis to determine subject matter jurisdiction over federal securities fraud claims?

3. Should the Court grant *certiorari* to review a decision that will not expand the territorial scope of the federal securities laws?

4. Should the Court grant *certiorari* to disturb twenty-five years of Circuit court decisions upholding the jurisdiction of the U.S. courts to regulate securities fraud in instances in

which fraudulent conduct either occurred in the United States or had substantial domestic effects?

STATEMENT OF THE CASE

A. Statement of Facts

The interlocutory order before the Court reinstated an action between two of the major competitors in the United States in the electronic security services business.[1] The action was commenced under the anti-fraud provisions of the federal securities laws to recover losses in excess of $100 million suffered by a single investor, A.D.T. Limited ("ADT"), arising from its investment, through its wholly-owned subsidiary, Itoba Limited ("Itoba"), in petitioner LEP Group plc ("LEP"). (A7)[2]

ADT, Itoba's parent, engages primarily in the businesses of providing security services (*i.e.*, residential and commercial property alarm systems) and conducting motor vehicle auctions in the United States and elsewhere. ADT's net sales in these two areas exceeded $1.2 billion for the year ended December 31, 1992. (JA438) ADT has thousands of shareholders, both record and beneficial owners, in the United States; as of May 1992, approximately 50 percent of ADT's common shares were held of record in the United States by

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[1] The facts set forth were current as of the date of the perfection of respondent's appeal to the Second Circuit in July, 1994. The material facts giving rise to the claims have not changed. We note that, within the past two months, petitioner LEP Group plc's security service subsidiary in the United States, National Guardian Corporation, has been sold.

[2] All references herein to "A__" are to pages of the Appendix to the Petition for a Writ of Certiorari filed by petitioners William R. Berkley and Peter J. Grant (hereinafter the "Berkley Pet."). All references herein to the "LEP Pet." refer to the Petition for Writ of Certiorari with Attached Appendix filed by petitioner LEP Group plc. All references to "JA___" are to pages of the Joint Appendix filed on the appeal before the Second Circuit.

over 2,000 record holders. (JA439) ADT's stock trades on the New York Stock Exchange. (JA439)

ADT has executive offices, which supervise its substantial North American operations, in Boca Raton, Florida, where its Chairman and its Chief Financial Officer maintain offices. (JA439) ADT conducts its extensive security services business in the United States through its wholly-owned subsidiary, ADT Securities Systems, a Delaware corporation. ADT is the largest single provider of central station monitoring security services in the United States, employing approximately 7,000 employees throughout the country. (JA438) Through its subsidiaries, ADT owns 55 offices in the United States. (JA462)

ADT's other principal business, conducting auctions for the sale and purchase of motor vehicles, employs approximately 3,100 persons in the United States on a full-time basis. (JA438) Thus, in total, ADT, through its wholly-owned subsidiaries, employs over 10,000 persons in the United States. (JA438, JA461)

LEP is a competitor of ADT in the United States, and, like ADT, is engaged extensively in the security and alarm services business, as well as the freight forwarding business. (JA741) LEP's security service business in the U.S. is conducted through its wholly-owned subsidiary the National Guardian Corporation ("National Guardian"), which is headquartered in Greenwich, Connecticut. National Guardian employs approximately 2,000 persons throughout the United States (JA690) and in 1989 had revenues of $200 million from its operations in the United States. (JA691)

LEP's securities trade in this country on the NASDAQ in the form of American Depository Shares ("ADS's"), representing American Depository Receipts ("ADR's") issued by an American depository in exchange for LEP's ordinary shares on deposit (each LEP ADR represents the bundling of five ordinary shares of LEP). (A7) As the Second Circuit

observed, there was a "direct linkage" between the trading price for LEP ordinary shares and LEP ADR's: "If the ordinary share price fell on the London Exchange, the market price of an ADR would decrease in similar manner, and vice versa." (A12) As a result of having registered its shares on the NASDAQ, LEP has subjected itself under Section 12(b)(1) of the Securities Exchange Act of 1934 [15 U.S.C. § 78l(b)(1)] to regular reporting requirements of the Securities and Exchange Commission (the "SEC").

LEP's investments in United States businesses include its substantial investment in real estate limited partnerships developing property in California and Nevada (JA692-96), and a trade finance company, Trading Alliance Corp. ("T.A.C."), headquartered in New York City. (JA697-99)

ADT's Interest in Investing in LEP and Its Analysis of the Company

ADT had acquired a relatively small amount of LEP securities as a result of the 1988 merger between LEP and National Guardian, in which ADT already held stock. ADT began to analyze potential further investments in LEP, with a view toward possibly acquiring National Guardian through an acquisition of LEP itself. (JA440-41)

In December, 1989, Michael Ashcroft, the Chairman of ADT, requested that Nicholas Wells, an ADT executive, undertake an evaluation of LEP in conjunction with Canadian Pacific, another company contemplating an investment in LEP. Wells had been hired by ADT to assist in managing its program of securities investments, and, as a result of his prior investment banking experience, was well-acquainted with techniques of valuation and investment analysis. (JA524-26)

Canadian Pacific had commissioned two companies to analyze and report on the business of LEP: S.G. Warburg, an investment bank, and LEK, a management consulting group. In December 1989 and January 1990, Nicholas Wells of ADT

met with representatives of Canadian Pacific, S.G. Warburg and LEK in order to discuss the reports produced by them, which had been provided to ADT. (JA526)

In performing his analysis of LEP, Wells, who was in charge of ADT's investigation of LEP, obtained and made extensive use of a report produced by S.G. Warburg (the "Report"). The Report was based heavily on LEP's filings with the SEC. As explicitly stated in the introduction to the Report:

> The analysis set out herein is based on publicly available information on [LEP], including recent U.K. annual reports and circular to shareholders, *the U.S. annual report on Form 20-F for the year ended 31st December, 1988 (the "Form 20-F")*, the company's shareholder register and brokers' reports. (JA534; emphasis added).

The Report given to Wells relied heavily on LEP's U.S. filings with the SEC, because as noted in the Report:

> In trying to analyze [LEP's] financial performance, the Form 20-F provides a more detailed description of the company's business activities than the U.K. accounts. (JA539)

The Report was not all that Wells studied. The disclosure documents themselves filed by LEP with the SEC in the United States were central to ADT's analysis of LEP. Wells was provided by Canadian Pacific with a copy of the LEP Form 20-F for the year ended 1988, which had been filed by LEP with the SEC on June 30, 1989. (JA594-670) As Mr. Wells stated in his affidavit before the District Court, "I regarded the LEP 1988 Form 20-F as highly significant for my analysis of LEP, as it was the most recent Form 20-F that had been filed by LEP." (JA527)

In March 1990, Canadian Pacific abandoned the idea of acquiring LEP jointly with ADT. ADT, however, remained

interested in exploring a strategic investment in LEP, and Mr. Wells continued his analysis of LEP. (JA527-28)

ADT's Decision to Purchase LEP Stock

David Hammond, Deputy Chairman of ADT, and Michael Ashcroft, the Chairman of ADT, conferred with ADT's Nicholas Wells regularly throughout the early part of 1990 regarding the progress of Mr. Wells' analysis of LEP and the conclusions he was formulating. (JA441-42, JA528)

In the Spring of 1990, Mr. Hammond discussed ADT's possible investment in LEP with Michael Ashcroft, the Chairman of ADT. Their discussion resulted in a decision that ADT would undertake a program of acquiring LEP stock. This decision was based largely on the analysis Mr. Wells had conducted of LEP, relying on LEP's U.S. filings with the SEC, such as its Form 20-F for 1988, and the Report commissioned by Canadian Pacific, which was also based on LEP's SEC filings. The contemplated stock acquisition program involved making purchases of LEP stock in the open market or through negotiated transactions as LEP stock became available, in such a way as to minimize the effect on the trading price of LEP stock. (JA442-43, JA672-73)

ADT decided to implement its purchase program through Itoba, one of its wholly-owned subsidiaries created to hold the investments of ADT. Itoba is a Channel Islands corporation formed by ADT to acquire and hold securities investments for ADT with funds provided by ADT. (*See* JA511-22.)[3]

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[3] Itoba's principal business, as disclosed in Schedules 13D filed by ADT with the SEC, is "to hold investments for A.D.T." (JA514) The significant investments by Itoba and ADT's other subsidiaries are identified in ADT's Annual Report and in its filings with the SEC as investments held *by ADT*, as opposed to the particular ADT subsidiary used to hold ADT's investment. For example, in ADT's Form 20-F for the year ended December 31, 1991, Itoba's investment in LEP is identified as an investment of ADT. (JA453)

In order to implement ADT's decision to invest in LEP, David Hammond contacted a member of the Itoba Board (which is elected by its sole shareholder, ADT), advised him of ADT's decision and recommended that Itoba acquire LEP stock on behalf of the ADT Group. Itoba adopted its parent corporation's recommendation ("[a]s expected," as the Second Circuit observed (A8)).

Itoba then implemented the ADT stock purchase program by contacting, in turn, William Grant, an ADT employee, and requesting that Mr. Grant commence making the purchases of LEP stock on behalf of Itoba. (JA686-87, JA444, JA672-73) Mr. Grant made the first purchase of LEP stock on June 4, 1990.

After the purchase program commenced, Mr. Wells continued his analysis of LEP. On or about June 29, 1990, LEP filed its Form 20-F for the year ended December 31, 1989. Mr. Wells obtained a copy of the 1989 Form 20-F in early July 1990, and he analyzed the disclosure contained in that Form 20-F to compare its information with that contained in the Form 20-F for the prior year (*i.e.*, 1988). Based upon this comparison, Mr. Wells concluded that there was no reason for ADT to abandon its ongoing program of acquiring LEP shares through Itoba (JA529), and the purchases continued.

ADT's Purchase of 7,300,000 LEP Shares Held by Defendant William Berkley

On October 8, 1990, ADT, through Itoba, purchased 7,300,000 LEP shares from petitioner William R. Berkley ("Berkley"), an American citizen and resident of Greenwich, Connecticut. David Hammond, ADT's Deputy Chairman, personally conducted the negotiation for this substantial purchase with Lehman Brothers Securities ("Lehman"), brokers he believed to be acting on behalf of Berkley. (JA445) As noted above, Berkley was a director of LEP and the president of its Connecticut subsidiary, National Guardian.

The Berkley transaction was set in motion when Berkley contacted his broker in Manhattan (New York & Foreign Securities Corporation) to arrange for the sale, which was cleared through Bear Stearns & Co. in New York. (JA705-06, JA59) Berkley's brokers, acting through Lehman's London branch, then contacted Mr. Hammond to inform ADT that 7,300,000 shares were being offered for sale by a United States-based holder of LEP stock. Through information from Lehman that the shareholder was based in the United States and was not selling his entire holdings of LEP stock, Mr. Hammond correctly concluded that the 7,300,000 shares that were being offered for sale were held by Berkley. (JA445) After negotiations with the broker over the price to be paid, Itoba purchased Berkley's 7,300,000 shares. Berkley, after paying his broker's commission, received $23,888,300 from the sale. (JA707-08, JA59)

With the purchase of the 7,300,000 shares from Berkley and several small purchases of LEP stock shortly thereafter, ADT suspended its purchase program in November 1990. ADT continued to analyze LEP for the purpose of considering whether to make a tender offer for LEP or otherwise to attempt to acquire National Guardian. (JA445)

Beginning in September, 1991 and continuing into 1992, LEP made a series of public disclosures that rocked the company and brought its stock value tumbling down. LEP disclosed for the first time that it had been making substantial, high risk investments and had engaged in previously undisclosed activities that were not central to its business. LEP wrote off $522 million in losses on its 1991 financial statements, a staggering result. (JA446, JA529-30) The most substantial part of the write-offs related to the previously undisclosed and unauthorized operation of a knitwear company conducted through LEP's New York-based trade finance subsidiary, T.A.C., and write-offs of its investment through the issuance of letters of credit in connection with real estate in California and Nevada.

LEP's current management has blamed former management for events that caused ADT's losses and has questioned the adequacy of prior public disclosures. At a meeting of LEP shareholders on August 24, 1992, David James, the new LEP Chairman, stated that it was "possible that the Board under my direction may wish to initiate legal actions regarding various matters which have led to a loss of shareholders' value in their Company" and (JA772-73) that "[s]hareholders may well feel it appropriate to enquire how such a series of calamities may have befallen their company in a relatively short period of time." (JA779) In response to a shareholder question at the meeting regarding non-disclosure in LEP's financial statements, Mr. James conceded that "the question of whether on occasions full and proper disclosure has been made is one which requires some subsequent and further review." (JA783)

The value of ADT's $114 million investment in LEP had plummeted to $2.26 million as of the commencement of this action in September, 1992, representing a loss of approximately $111 million. (A9) This loss was borne by ADT's numerous U.S. shareholders (A15), as ADT has written off on its own balance sheet the entire amount of its $114 million investment in LEP. (JA903)

In the wake of these disclosures, ADT decided to commence this action. The Complaint, filed on September 22, 1992 in the name of its subsidiary Itoba, asserts claims against all defendants pursuant to Section 10(b) of the Securities Exchange Act of 1934 [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5], to recover damages arising from defendants' fraudulent non-disclosure in filings made by LEP with the SEC. (JA38, JA42-44) In addition to the claims asserted against LEP and against its directors as Section 20(a) "controlling persons" under Section 10(b) and Rule 10b-5, Itoba asserts independent claims for federal securities violations against petitioner Berkley arising out of his personal sale of LEP securities for over $23 million. (A9)

B. The Proceedings Below

Itoba commenced this action on September 22, 1992 in the United States District Court for the District of Connecticut. On February 4, 1994, a Magistrate Judge rendered a Recommended Ruling, recommending that the District Judge grant petitioners' motions to dismiss for lack of subject matter jurisdiction. (A22-35) On March 14, 1994, the District Judge, in a one-sentence Endorsement Order, over Itoba's objection adopted the Recommended Ruling of the Magistrate Judge. (A21)

On May 15, 1995, the Second Circuit, in a unanimous decision, reversed the District Court's order of dismissal, remanding the action to the District Court for further proceedings. Petitioners filed a petition for rehearing with a suggestion for rehearing *en banc*, which was denied by the Second Circuit on July 14, 1995. (A1-2) LEP Group plc, William R. Berkley and Peter J. Grant filed petitions for writ of *certiorari* on or about October 12, 1995; defendants John L. Read and John R. East have not sought *certiorari*. On October 12, 1995 and November 3, 1995, petitioners filed motions with the District Court to dismiss the action on the grounds of *forum non conveniens*. Those motions are pending.

REASONS FOR DENYING THE WRIT

I.

IN VIEW OF THE SECOND CIRCUIT'S REMAND FOR FURTHER DEVELOPMENT OF JURISDICTIONAL FACTS, THE SUPREME COURT SHOULD NOT REVIEW THIS INTERLOCUTORY DECISION

The decision that petitioners urge this Court to review is interlocutory. In reversing the District Court's dismissal for lack of subject matter jurisdiction, the Second Circuit remanded for "a trial on the merits in which the facts relevant to jurisdiction may be more fully developed." (A18)

The Second Circuit also took particular note of the Magistrate Judge's erroneous factual findings on which the District Court had based its decision, including the erroneous finding that neither ADT nor Itoba had read and relied on LEP's SEC filings in making their purchase decision. (A11) Among the additional facts related to jurisdiction that the Second Circuit left for development on remand is whether the sale by Berkley of 7,300,000 shares of LEP stock through a New York broker and the purchase of such shares by Itoba on the same day was "coincidental."[4] (A16)

Thus, the Court is confronted with an interlocutory order based on a disputed and, in some respects, undeveloped factual record. The well-settled jurisprudence of this Court points clearly to the denial of *certiorari* to review such an order. *See Virginia Military Institute v. United States*, U.S. ___, 113 S.Ct. 2431, 2432 (1993) (Scalia, J., concurring) ("We generally await final judgment in the lower courts before exercising our *certiorari* jurisdiction"). Issuance of a writ of *certiorari* in cases presented for review of interlocutory orders is confined to instances in which review "is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause." *American Construction Co. v. Jacksonville, T. & K.W.R. Co.*, 148 U.S. 372, 384 (1893). "[E]xcept in extraordinary cases, the writ is not issued until final decree." *Hamilton-Brown Shoe Co. v. Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916).

There is yet another procedural reason why the Court should decline to review the Second Circuit's interlocutory order—one which illustrates the wisdom of declining review of interlocutory orders. On October 12 and November 3, 1995, petitioners moved in the District Court for dismissal of this action on the ground of *forum non conveniens*. While

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[4] Itoba contended below that Berkley's sale and Itoba's purchase constituted effectively a direct sale from Berkley to Itoba; Berkley contended that he sold his shares on the market, to no purchaser in particular.

Itoba is opposing the motions, the District Court's determination could dispose of this action prior to the opportunity for review by this Court. Adherence in this case to the Court's general rule declining the review of interlocutory orders would prevent potentially unnecessary review by this Court. Petitioners, of course, will have the opportunity to seek a full review of any jurisdictional issues should the *forum non conveniens* motions be denied and a judgment in Itoba's favor be rendered at trial.

II.

PETITIONERS HAVE SKEWED THE RECORD TO OBSCURE SUBSTANTIAL CONDUCT AND EFFECTS WITHIN THE UNITED STATES

Not surprisingly, petitioners seek to characterize this action as entirely "foreign." (*See* Berkley Pet. at 4 ("foreign purchases of foreign securities on foreign exchanges . . ."); LEP Pet. at 2 (same).) However, the Second Circuit appropriately cut through petitioners' attempts to obscure the substantial conduct by defendants, and effects of defendants' actions, within the United States, which satisfy the well-settled "Conduct Test" and "Effects Test" for subject matter jurisdiction. The significantly domestic nature of the conduct and effects is apparent from the following facts recognized by the Second Circuit:

1. The alleged fraud culminated with LEP's filing with the SEC in Washington, D.C. of documents containing material misrepresentations and omissions. (A13) Thus, this is not the kind of case appropriately screened by the Conduct Test, in which defendants have engaged in a fraud abroad and, along the way, have engaged in some "merely preparatory" activity within the U.S. borders before the fraud is consummated abroad.

2. As discussed within, because LEP has elected to take advantage of U.S. markets by trading its securities on the NASDAQ (A7), LEP is required to make regular disclosures in filings with the SEC under Section 12(b)(1) of the Securities Exchange Act of 1934 [15 U.S.C. § 78l(b)(1)].

3. ADT sought out and relied on LEP's SEC filings in making its decision to invest over $100 million in LEP. (A11)

4. Consistent with its precedents focusing on the economic substance of a transaction for the determination of jurisdiction (*see Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326 (2d Cir. 1972)), the Second Circuit observed that the investment in LEP securities at issue was made, and the loss incurred, by Itoba's parent company, ADT, a company whose shares are listed on the New York Stock Exchange and roughly 50 percent of whose shareholders of record reside in the United States. (A7)

5. Perhaps the most glaring of petitioners' omissions is the absence of any discussion concerning the claim against petitioner William R. Berkley, a United States citizen working and residing in Greenwich, Connecticut, who was a director of LEP and the President of its U.S. subsidiary, National Guardian. His personal sale originating in Greenwich, Connecticut of over $23 million in LEP securities, which were purchased by Itoba, forms the basis of a sizeable portion of Itoba's claim for damages on its federal securities fraud claims. (A9, A16-17)

Such substantial conduct and effects within the United States, completely ignored by petitioners, satisfy the requirements for subject matter jurisdiction under the well-settled "Conduct Test" and "Effects Tests," as discussed in Point III.

III.

THERE IS NO CONFLICT AMONG THE CIRCUITS

In an attempt to create the appearance of a substantial conflict among the Circuits, petitioners, at great length, describe past applications of the "Conduct Test" and the "Effects Test" by different Circuits. (Berkley Pet. at 8-17.) However, more than anything else, petitioners' argument demonstrates not a conflict among the Circuits, but only differences in emphasis in their application of these tests.

All of the Circuits, without exception, apply a Conduct Test/Effects Test analysis for the determination of subject matter jurisdiction—an analysis originating in the Second Circuit's decision in *Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir. 1968), *cert. denied sub nom. Manley v. Schoenbaum*, 395 U.S. 906 (1969), and applied by the Second Circuit in this case. And in most cases, the result of the analysis by the different Circuits to a given set of facts would yield the same conclusion: either finding jurisdiction or finding it lacking.

Although various Circuit courts have developed somewhat different formulations of the Conduct Test/Effects Test, no "conflict" exists among the Circuits within the meaning applied by this Court. As a commentator of this Court's *certiorari* jurisprudence has observed, a conflict for the purposes of a *certiorari* petition "means that there must be a real or 'intolerable' conflict on the same matter of law or fact, not merely an inconsistency in dicta or in the general principles utilized." R. Stern *et al.*, *Supreme Court Practice*, § 4.3 at 167 (1993).[5]

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[5] *See, e.g.*, *United States v. Lorenzetti*, 467 U.S. 167, 173 (1984) (interpretation of federal statute by the Sixth Circuit and the Third Circuit was "squarely inconsistent"); *Ins. Corp. of Ireland v. Compagnie de Bauxites de Guinee*, 456 U.S. 694, 700 (1982) (Third Circuit's decision that a discovery sanction imposing finding of personal jurisdiction did not violate due process "directly conflict[ed]" Fifth Circuit decision); *see also Commissioner v. Scottish Amer. Inv. Co.*, 323 U.S. 119, 121 (1944) ("The irreconcilable conflict between the two courts below led us to grant certiorari.")

On repeated occasions, *certiorari* has been sought to review Circuit court decisions finding subject matter jurisdiction over federal securities fraud claims involving foreign aspects. In each case, this Court has denied *certiorari*.[6] And in *SEC v. Kasser*, 548 F.2d 109 (3d Cir.), *cert. denied sub nom. Churchill Forest Industries (Manitoba) Ltd. v. Securities and Exchange Comm'n*, 431 U.S. 938 (1977), the petitioners sought *certiorari*, arguing, just as petitioners have in this case, that *certiorari* should be granted to resolve an alleged conflict between the Third, Second, Eighth and Ninth Circuits as to the proper standard for subject matter jurisdiction over federal securities fraud claims involving foreign elements. Yet, this Court denied *certiorari*. *Kasser*, *supra*, 431 U.S. 938 (1978).

Much of petitioners' argument relating to conflict is based on their claim that the Second Circuit, in *Itoba*, departed from its own restrictive Conduct Tests/Effects Test formulation, thereby expanding the continuum between those Circuits adhering to the most restrictive formulation and those adopting the most expansive. This suggestion is simply not so.

As petitioners concede, the Second Circuit jurisdictional test has always been among the most restrictive. In this case, the Second Circuit's discussion of the jurisdictional issue is mostly a pointed analysis of how the District Court misread critical facts before it on the jurisdictional motion. In discussing these facts in relation to the Conduct Test and Effects Test, the Court did not create a new formulation; it simply applied its tests to the facts before it.

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[6] *See Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir. 1968), *cert. denied sub nom. Manley v. Schoenbaum*, 395 U.S. 906 (1969). *SEC v. Kasser*, 548 F.2d 109 (3d Cir.), *cert. denied sub nom. Churchill Forest Industries (Manitoba), Ltd. v. Securities and Exchange Comm.*, 431 U.S. 938 (1977); *Alfadda v. Fenn*, 935 F.2d 475 (2d Cir.), *cert. denied*, 502 U.S. 1005 (1991); *Tamari v. Bache & Co. (Lebanon) S.A.L.*, 730 F.2d 1103 (7th Cir.), *cert. denied*, 469 U.S. 871 (1984) (claims under the anti-fraud provisions of the Commodities Exchange Act).

In discussing the Conduct Test, the Court set forth its traditional formulation, citing *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974 (2d Cir.), *cert. denied sub nom. Bersch v. Arthur Andersen & Co.*, 423 U.S. 1018 (1975) and *Alfadda v. Fenn*, 935 F.2d 475 (2d Cir.), *cert. denied*, 502 U.S. 1005 (1991). (A10) The Court then rejected the District Court's finding that LEP's United States-based activities did not "directly cause" Itoba's financial losses. (A11) Again applying its familiar test, the Second Circuit also found that the filing of fraudulent SEC filings in Washington, D.C. constitutes fraudulent activity in this country that is not "merely preparatory" to a fraud committed outside the United States. (A13-15) Nowhere did the Second Circuit say, or suggest, that it was changing its test or that Itoba failed to meet its traditional Conduct Test.

Similarly, in applying the Effects Test, the Second Circuit broke no new ground. Rather, the Court emphasized that the District Court erred in finding the Effects Test not met merely because Itoba, and not ADT, was the plaintiff. (A15-A16)

Much of petitioners' argument focuses on the Second Circuit's observation that, with respect to the Conduct Test and the Effects Test, "an admixture or combination of the two often gives a better picture of whether there is sufficient United States involvement to justify the exercise of jurisdiction by an American court." (A10) To suggest that this observation represents either a fundamental shift in Second Circuit jurisprudence, or a major change in subject matter jurisdiction jurisprudence when taken in context of other Circuit court decisions—all of which differ slightly in their formulation of the Conduct Test/Effects Test analysis—is to grossly exaggerate the implication of that observation.[7]

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[7] Even assuming *arguendo* that *Itoba* created a new formulation of the Conduct Test/Effects Test analysis, it is by no means clear that the formulation would expand jurisdiction. Just as elements which would not independently satisfy the Conduct Test or Effects Test might, in combination, produce a finding of jurisdiction, where a showing of *either* conduct or effects is particularly weak, a court might decline jurisdiction under *Itoba*.

Petitioners' conflict argument merely shows that in a particular case, subject matter jurisdiction theoretically could exist under the formulation of one Circuit and not the other. However, because of the substantial overlap of the Conduct Test/Effects Test analysis as applied in every Circuit, the nuances among the Circuits' formulations do not create a conflict that justifies granting *certiorari*.

Finally, whatever the differences among the Circuits, this case would serve as a poor vehicle for this Court to speak on the issue of subject matter jurisdiction. This is not a "close" case, in which one particular Circuit court's formulation would support jurisdiction while another's would preclude it. Because this case would pass muster under the most restrictive formulation (that applied by the Second Circuit and D.C. Circuit), there is no question that jurisdiction would be found in Circuits which, as petitioners recognize, have a more expansive view of jurisdiction.[8]

IV.

THE SECOND CIRCUIT'S DECISION WILL NOT OPEN THE FLOODGATES TO FEDERAL SECURITIES ACTIONS LACKING SUBSTANTIAL CONDUCT OR EFFECTS WITHIN THE UNITED STATES

Petitioners contend that:

> The Second Circuit decision threatens to open the doors of the United States courts to foreign purchasers of foreign securities on foreign exchanges that the United States has little interest in regulating.

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[8] Petitioners misleadingly suggest that the Second Circuit's reference to "questionable law" is a criticism of its own subject matter jurisdiction jurisprudence. (Berkley Pet. at 16.) As apparent from the context of the reference, the Second Circuit was merely referring to the Magistrate Judge's misapplication of Second Circuit precedent.

Berkley Pet. at 4. Indeed, petitioner LEP goes so far as to say:

> [T]he Court of Appeals has created a new doctrine under which any foreign corporation must anticipate that any purchaser of its securities, anywhere in the world, who received advice from anyone, American or not, which was derived in any manner and at any level of indirectness from information that appeared in an SEC filing, can sue in an American court, provided some shareholder of the purchaser (or as in this case a shareholder of the purchaser's corporate parent) is American.

(LEP Pet. at 10-11.)

Petitioners' dire prediction that this decision will produce a flood of Rule 10b-5 actions is sheer speculation, unsupported by any empirical evidence, and, of course, any history. Should this prediction prove true, there is time enough for this Court to revisit the issue, and to evaluate both the number of those filings and the quality of those actions when measured against the purposes underlying the U.S. securities laws. However, the reality is that the facts supporting jurisdiction in this case could not be alleged by the myriad, hypothetical plaintiffs who petitioners claim will flood this country's courts in the wake of the *Itoba* decision. Petitioners' arguments completely overlook the substantial conduct and effects within the United States in this case, which few putative Rule 10b-5 plaintiffs will be able to allege, let alone prove.

In their briefs below, petitioners made many of the same doomsday arguments they have made here. The Second Circuit correctly contrasted ADT's circumstances from those of the many plaintiffs that petitioners speculate will overwhelm our courts: "Unlike some securities actions brought to recover questionable damages on behalf of optimistically described classes, *we are met here with a single plaintiff which suffered direct substantial losses*." (A17; emphasis added) Similarly, the Second Circuit correctly distinguished

this case from a fraud on the market case in which a plaintiff would not allege actual reliance on SEC filings. (A14) Only the plaintiff who can allege facts showing actual reliance will find support in the holding in *Itoba* as a basis for subject matter jurisdiction.

Petitioners also suggest that a defendant's fraudulent filings with the SEC are an insufficient or unpredictable basis for subject matter jurisdiction. (See Berkley Pet. at 25 ("Any investor claiming that a foreign market was somehow influenced by an ADR filing would now be entitled to a United States forum.")) Petitioner LEP asserts that now "nearly every foreign transaction of securities involving a company with some connection to the United States will subject all parties to the transaction to the prospect of litigation in the United States." (LEP Pet. at 22.)

However, LEP is hardly "a company with some connection to the United States." LEP, through its wholly-owned U.S. subsidiary National Guardian, was one of the major providers of electronic security services in the United States. Moreover, LEP had taken the significant step of registering its securities on the NASDAQ, which the SEC treats for reporting purposes as a "national exchange." As petitioner LEP itself points out, the Securities Exchange Act of 1934 (the "Exchange Act"), in its statement of legislative purpose, expresses Congress' concern with the "national market system," citing 15 U.S.C. § 78b. (LEP Pet. at 12.) As a result of availing itself of the benefits of trading on the NASDAQ, LEP was required to register its ADR's with the SEC pursuant to Section 12(b)(1) of the Exchange Act [15 U.S.C. § 78(l)(b)(1)].[9]

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[9] By registering its securities on the NASDAQ, LEP lost the benefit of an exemption for registration enjoyed by many foreign corporations whose securities trade in this country as ADR's *but do not trade on a national exchange*. Section 12(g) of the Exchange Act [15 U.S.C. § 78l(g)]and the regulations thereunder provide a lower tier "information-supplying" exemption for companies whose securities do not trade on a national exchange. This exemption establishes a system of supplying

There is nothing inappropriate, unbounded or unpredictable about subjecting to the anti-fraud provisions of the federal securities laws a company that has elected to register its securities on a U.S. national market system like the NASDAQ. Companies with "merely some connection to the United States," for whom LEP purports to express concern, need not fear being haled into the U.S. courts in the wake of the *Itoba* decision.

Petitioners also suggest that the holding in this case would allow jurisdiction so long as "some shareholder of the purchaser (or as in this case, of the purchaser's corporate parent) is American." (LEP Pet. at 11.) Jurisdiction was not found merely because "some shareholder . . . [was] American." The Second Circuit found that [h]ere, we have fraud occurring on an American exchange that has impacted detrimentally *upon thousands of United States shareholders* in the defrauded company, *i.e.*, over $100 million lost in the shareholders' corporate equity." (emphasis supplied) (A15) Allowing jurisdiction on these facts will not open the floodgates to litigation.

If anything, the Second Circuit's analysis in *Itoba* ensures that subject matter jurisdiction will not be found in cases lacking significant conduct in, or effects within, the United States. By considering an "admixture or combination" of the

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information that is less rigorous than the periodic reporting requirements of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] to which LEP is subject. When a foreign issuer has its ADR's listed for trading on NASDAQ, as LEP has done, it becomes subject to the more rigorous reporting requirements under Section 13(a) of the Exchange Act. The "information-supplying" exemption was made unavailable to foreign issuers whose securities trade on NASDAQ because:

> [T]he [SEC] believes that foreign securities included in NASDAQ should be regarded prospectively as voluntarily seeking U.S. trading markets and hence should be denied the information supplying exemption.

Securities Act Release No. 6493, [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶83,435 at 86,295 (Oct. 6, 1983).

Conduct Test and the Effects Test (A10), the Court can decline jurisdiction if there is a troubling gap in the level of either U.S. conduct or U.S. effects.

V.

THIS COURT SHOULD NOT GRANT *CERTIORARI* BASED ON LEP'S SUGGESTION THAT THERE SHOULD BE NO EXTRATERRITORIAL APPLICATION OF THE FEDERAL SECURITIES LAWS

Not content with suggesting a conflict among the Circuits, LEP asserts that the federal securities laws should never be given extraterritorial effect. (LEP Pet. at 11-12.) This argument would overturn not only the decision in this case, but would reverse the law of all the Circuits, which, without exception, determine the existence of subject matter jurisdiction under the Conduct Test/Effects Test analysis.

The characterization of the jurisdictional issue as the "extraterritorial" application of the U.S. securities laws is somewhat of a misnomer to the extent it implies that a federal court would exercise jurisdiction over a purely foreign dispute. Traditionally, the term has been applied to disputes in which *some*—not all—of the relevant conduct or transactions has occurred abroad; were the conduct or transactions at issue to be entirely "extraterritorial," the issue of purported U.S. jurisdiction would never arise. Therefore, in any given case, the issue is not whether the court should exercise jurisdiction over a purely foreign dispute, but whether the conduct or effects within the United States are sufficient to justify the assertion of jurisdiction.

LEP bases its argument against any extraterritorial application of the federal securities fraud laws on its assertion that "[t]he language of the Exchange Act does not directly disclose any intention to give it extraterritorial affect [sic]" (LEP Pet at 11.) In *Tamari v. Bache & Co. (Lebanon) S.A.L.*, the

petitioners for *certiorari* made the same argument LEP makes in this case, and this Court denied *certiorari*. See *Tamari v. Bache & Co. (Lebanon) S.A.L.*, 469 U.S. 871 (1984) (*certiorari* petition argued that the Seventh Circuit had erred by applying the Conduct Test and Effects Test).

Through the development of the Conduct Test/Effects Test analysis, the Circuit courts, led by the Second Circuit, have applied the federal securities laws to provide a remedy for fraudulent conduct in this country injuring foreigners (so long as that conduct is not "merely preparatory" to the fraud), and fraudulent conduct causing a "substantial effect" within the United States. *See generally, Alfadda, supra,* 935 F.2d at 478. The Second Circuit, followed by every Circuit Court considering the question, has applied a Conduct Test/Effects Test analysis so that American courts would not be powerless to prevent "the United States [from] be[ing] used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners." *IIT v. Vencap.*, 519 F.2d 1001, 1017 (2d Cir. 1975). Petitioners point to no substantial source of dissatisfaction from the Congress, the courts or any of the foreign governments for whom petitioners express concern. Twenty-five years of this settled and workable jurisprudence should not be lightly cast aside.

CONCLUSION

For the foregoing reasons, the Petitions for Writ of *Certiorari* filed by LEP Group plc, William R. Berkley and Peter J. Grant should be denied.

Respectfully submitted,

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—and—

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